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IN THE

Supreme Court of the United States

October Term 1960

No. 245

CHARLES B. SMITH, as Special Administrator of the Estate of Edward S. Birn, Deceased,

Petitioner,

vs.

MILTON SPERLING, JACK L. WARNER, UNITED STATES PICTURES, INC., WARNER BROS. PICTURES, INC., and HERBERT FRESTON, MILTON SPERLING, REA E. WARNER and DORIS WARNER VIDOR as Executors of the Estate of Harry M. Warner, Deceased,

Respondents.

Brief of Jack L. Warner, Warner Bros. Pictures, Inc., and the Executors of the Estate of Harry M. Warner, Deceased, in Opposition to Petition for Certiorari.

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MILTON SPERLING, JACK L. WARNER, UNITED STATES PICTURES, INC., WARNER BROS. PICTURES, INC., and HERBERT KRALTON, MILTON SPERLING, JACK L. WARNER and LOUIS W. ORNER, WILLIAM as Executors of the Estate of Harry M. Warner, Deceased,

Respondents.

Brief of Respondents, Warner Bros. Pictures, Inc., Jack L. Warner, and the Executors of the Estate of Harry M. Warner, Deceased, in Opposition to Petition for Writ of Certiorari.

The Petitioner seeks review of a decision of the Court of Appeals for the Ninth Circuit affirming a judgment of dismissal by the District Court in a shareholder's derivative suit. Federal jurisdiction is based upon diversity of citizenship. The question of federal jurisdiction in this case was decided by this Court in 1957 (*Smith v. Sperling*, 354 U. S. 91, 1 L. Ed. 2d 1205, 77 S. Ct. 1112). Pursuant to the applicable mandates of this Court and of the Court of Appeals hereon, the trial was resumed in April 1958, at which time it was stipulated that all evidence theretofore taken in the 1954 trial should be considered, and addi-

tional evidence was taken. Findings and judgment adverse to the Petitioner were made in December 1958. The Petitioner then appealed to the Court of Appeals which affirmed; its opinion, rendered April 1960, being reported in 277 F. 2d 634. A copy appears in the Appendix to the Petition herein, and in the Transcript of Record hereon, pages 842 to 845 inclusive. References will be to such copy in the record.

Though the Petition does not anywhere so state, or even indicate, the judgment below covers two separate aspects as to which the dispositions were different. The basic claim had been made by Petitioner that the contracts between the corporate Defendants were invalid and should be set aside as having been obtained through the improper influence of the individual brothers Warner. Up to the time of the decision by this Court on the question of jurisdiction in 1957, this claim, which alone is reflected in the pleadings, was the sole claim. The present judgment of the District Court and the decision of the Court of Appeals dispose of that basic issue completely and on the merits. Subsequent to the remand by this Court and during the 1958 trial, Petitioner sought to show that there had been maladministration and certain accounting and interpretive errors of and under those contracts. It was with respect to these subsequent claims, differing in nature from the original and basic contention, that the trial court determined that Petitioner was precluded from asserting such claims under state laws that he had no standing to maintain the claims in the face of a decision by the Board of Directors of Warner that it was not in the interest of the Corporation to sanction the effort of the Petitioner with respect to those claims. The judgment was, therefore, that of dismissal on the mer-

its of the basic claim, but without determination of the merits of such subsequent claims.

Since we do not believe that the questions actually involved in this case are those set forth in the Petition, and since we do not believe the status and posture of the case have been adequately or fairly set forth in the Petition to enable the true questions to be evident, we feel it necessary at this point to restate the situation. It is submitted that an appreciation of the actual situation will show only that Petitioner disagrees with the Court of Appeals on the question of whether the evidence supports the Findings upon which the judgment is based.

Statement of the Case.

On the former presentation to this Court only the issue of jurisdiction was present, but in connection therewith there had been a lengthy trial resulting in Findings of Fact adverse to the Petitioner upon the question of the existence of fraud or other improper influence in the establishment of the contractual relationship between Warner and United. This Court noted (354 U. S. 91 at 95) that:

> "The gist of the findings of the District Court is that since there was no fraud on the part of the directors in making the contracts but only an exercise of independent business judgment, the management was not antagonistic to the financial interests of the corporation."

The facts, so found after a preliminary trial, were deemed by this Court to go to the merits and to be inapplicable in their relationship to and effect upon federal jurisdiction. It held that for the establishment of

jurisdiction, the matter of "antagonism" was to be determined from the face of the pleadings and the nature of the controversy (354 U. S. 91 at 96).

At the second hearing in 1958, since the first hearing had been extensive and the facts there adduced, and erroneously applied by the trial court on the matter of jurisdiction, were directly relevant on the merits, it was stipulated that all the evidence at the first hearing should be considered on the merits [R. 699; Op., R. 844]. At such 1958 hearing much additional evidence was presented, most of which related to the subsequent claims already mentioned. The facts relating to the claim of basic invalidity of the contracts remained and now remain substantially the same as they had been presented in 1953, but have been applied to determine the validity of the contracts instead of the question of federal jurisdiction. With respect to the facts, the Court of Appeals has twice examined the record, and each time determined that the evidence supported the Findings. It so stated on the first appeal (237 F. 2d 317 at 325(9)). On the second appeal the Court of Appeals said [R. 844]:

> "On the findings of fact by the district court, which seem to us to be adequately supported by the evidence, we think that the district court's judgment of dismissal was inevitable and correct."

With respect to the first aspect of the case, *i.e.*, the validity of the contract, and which issue was and is the only one presented by the pleadings, the District Court found that such contracts had been made with the approval of the Board of Directors of Wismer, that such Board was free from control or domination by

the individual Defendants named, had been considered in good faith by the Board and approved in the exercise of its independent business judgment without fraud, coercion or domination. In addition, it found the vital fact that the contracts themselves were fair and reasonable [Finding XXV, R. 612, 613] For convenience, a copy of Finding XXV is printed in the Appendix hereto.

At the close of its former opinion in this case, this Court said (354 U. S. 91 at 97):

> "A trial may demonstrate that the stockholder is wrong and the management right. It may show a dispute that lies in the penumbra of business judgment unaffected by fraud. But that issue goes to the merits; not to jurisdiction."

This is exactly what did happen with respect to basic validity. The evidence did demonstrate that the Petitioner was wrong and the corporation was right, and that the contracts were not only fair, reasonable and free of impropriety, but were also very lucrative to Warner. Such trial also showed that both the making of the contracts and the refusal years later to sanction this suit were proper exercises of business judgment.

With respect to the second portion of the case involving the subsequent claims of accounting error and maladministration, the trial court found [Finding XXVI, R. 613, 614] that during the trial the Petitioner had raised issues not presented by the pleadings relating to matters of interpretation of the contracts and accounting practices and lists those claims in essence. The story of the presentment of those claims to the 1958 Board of Directors of Warner is described fully

by the trial court in Finding XXVI [R. 614-617 incl.]. This Finding shows that in 1958, during the trial, Petitioner did present these subsequent claims in writing to the Board of Directors, but such Board employed the law firm of Dewey, Ballantine, Bushby, Palmer & Irvine (of New York) to investigate the law and facts involved and advise the Board, and that after receiving the report and advice of these consultants, the Board formally determined that it was not of the best interests of the corporation to sanction the efforts of the Petitioner in connection therewith. The Finding names the seven members of such Board who unanimously took such action. Neither Jack L. Warner nor Albert Warner participated. (Note: Harry M. Warner was then deceased.) As part of that Finding and with respect to that action, the trial court also determined that in so doing the Board acted in good faith without fraud, coercion or domination, in the interests of the corporation and in the exercise of proper independent business judgment. This portion of Finding XXVI is quoted in the Opinion of the Court of Appeals herein [R. 845, and Op. App. Pet. p. 4]. A copy of this Finding XXVI is printed in the Appendix hereto for the convenience of this Court.

It was with respect to the subsequent matters considered in Finding XXVI that the Court concluded that the Petitioner as the Plaintiff under such circumstances, had no right or standing to sue derivatively [R. 618, Conclusion of Law V].

We further believe it well to point out that the Court of Appeals in its Opinion specifically noted that the contracts and the operations thereunder had proved to be very lucrative to Warner Bros. Pictures, Inc.,

and that with relation to the asserted claims involving accounting practices, the firm of Price Waterhouse & Co. had been the independent auditors for each of the corporations, and that the accounting practices of each were in accordance with the practices acceptable in the industry [R. 844-845]. These views of the Court of Appeals show its belief that the business judgment of the Board of Directors had been good, and also and even though the trial court had not decided the merits of the subsequent claims, that such claims actually had little merit. There was no evidence whatever showing or tending to show that if any such errors in administration had actually occurred, they had been made "purposefully" to enrich United as Petitioner asserts (*cf.* Pet. p. 6).

Questions Presented.

The Petition herein does not reflect any of the typical grounds for Certiorari suggested in Rule 19 or otherwise recognized by this Court, but only a desire that this Court reconsider the evidence and accept Petitioner's version thereof. The question, therefore, is whether this Court should grant Certiorari to review a very extensive record and determine whether the evidence supports the Findings, after the Court of Appeals has twice examined that record and determined that such Findings had adequate support, when such Findings have determined

(a) that the basic contracts had been made and entered into in good faith, were fair and reasonable, were intended to be and were considered by the Board of Directors of the corporation to be sound business arrangements for the best present

and future interests of the corporation, and that such Board had not been affected by fraud or subjected to coercion or improper domination, and

(b) that the subsequent claims, relating to asserted accounting and administrative errors, had been presented to and considered by the Board of Directors, and such Directors had in good faith, without fraud, coercion or domination, acting in the interests of their corporation and in their independent business judgment, declined to sanction the prosecution of such claims by the Petitioner."

ARGUMENT.

The facts as found are clear and complete with respect to each aspect of this case. There remains to be considered only what is the law applicable to those facts, and whether those facts, in the light of the law, justify the judgment. If they do, as we shall show herein, then it is plain that Petitioner is seeking merely a reconsideration of the evidence in an effort to obtain different Findings.

I.

The Governing Substantive Law Is State Law.

In this case, as in any stockholder's derivative action, the governing substantive law is state law. This Court in its former Opinion herein said (354 U. S. 95),

"'Since our decision in *Erie R. Co. v. Tompkins*, 304 U. S. 64, the law which governs the merits in these derivative actions is local law. *Cohen v. Beneficial Industrial Loan Corp.*, 337 U. S. 541, 555, 556.'"

II.

The Judgment Here Is In Accordance With State Law (A) on the Merits as to the Basic Validity of the Contracts, and (B) on the Right of the Plaintiff to Maintain the Action With Respect to the Subsequent Claims.

(A) The Basic Contracts.

The basic contract made in 1945 and the subsequent amendments thereof were found to be fair and reasonable and in the financial interests of the corporation. They were entered into in good faith, and the action of the Board of Directors of Warner in approving them was found to be free of fraud, coercion or improper influence or domination by the individual defendants, and a proper and independent exercise by the Board of its discretion. [Findings XIV, R. 600-605; XVII, R. 606; XXII, R. 610-611; XXV, R. 612-613.] The facts so found with respect to the contracts justify the judgment under the requirements and standards of any and all of the state decisions or their federal counterparts which are cited by Petitioner or which are discussed herein. Such authorities, being primarily presented by Petitioner in connection with the so-called subsequent claims, are best considered in connection with that aspect of the case.

(B) The Subsequent Claims.

With respect to the subsequent claims, the Courts below have concluded that the Petitioner is not entitled to proceed on behalf of Warner in the prosecution thereof. In attacking this result, Petitioner purports to state his contentions in the Court Below (Pet. pp. 15 [illegible] and if such statement is intended as an argu-

at anyone's instigation. Furthermore, with respect to the Bernhard payment, the record shows that for a long time the practice of Warner had been to provide six-months' severance pay for executive employees who had been with the company for many years [R. 451], that Bernhard had been with the company for at least 15 years [R. 339 and 472], and that Bernhard's salary at the time of severance was $3,000.00 per week [R. 333]. Such payment was made in accordance with practice to a person qualified under that practice, and the amount was in accordance with that practice.

The issue upon the relevant Findings is whether Petitioner had a right to maintain the action. The action was brought and has been twice tried in California. California is the state of the forum, and the question as to whether an action can be maintained in California is peculiarly a matter of California law. However, with respect to the right of a shareholder to maintain a derivative suit, the laws of California and Delaware, as well as the general federal concept, adopt the same theories, standards and determinative elements, all of which are met by the Findings herein.

(a) *The California Cases.*

The law of California directly relevant to the matter is clearly set forth in *Findley v. Garrett* (1952), 109 Cal. App. 2d 168, 240 P. 2d 424; and *Fornaser v. Cosmosart Realty & Bldg. Corp.* (1929), 96 Cal. App. 549, 274 Pac. 597. A Petition For Hearing by the Supreme Court of California in the *Findley* case was denied (109 Cal. App. 2d at 180), and the case was commented upon with approval in *Olson v. Basic Oil Co.* (1955), 136 Cal. App. 2d 543 at 550; 288 P. 2d 952 at 962; where the rule of *Findley* is described

as "wholesome." No decisions adversely criticizing *Findley* have been found.

In *Findley v. Clarence*, *supra*, the court said (100 Cal. App. 2d 186 at 174, 240 Pac. 421 at 426):

> "The power to manage the affairs of a corporation is vested in the board of directors. (*Scott v. Los Angeles Mountain Park Co.*, 92 Cal. App. 258, 264 [267 P. 914].) Where a board of directors, in refusing to commence an action to redress an alleged wrong against a corporation, acts in good faith within the scope of its discretionary power and reasonably believes its refusal to commence the action is good business judgment in the best interests of the corporation a stockholder is not authorized to interfere with such discretion by commencing the action. (See *Bramhall v. Consumers Brick & Tile Co.*, 96 Cal. App. 540, 557 [274 P. 597].)"

and at pages 177-178 (Cal.) and 428 (Pac.):

> "Directors have the same discretion with respect to the prosecution of claims on behalf of the corporation as they have in other business matters. In this respect the fact that a claim may be founded in fraud does not differentiate it from other claims. Refusal to sue on a fraud claim is not, as plaintiffs contend, a ratification of fraud. The mere fact that a recovery for the corporation would probably result from litigation does not require that an action be commenced to enforce the claim. Even if it appeared to the directors of Douglas that at the end of protracted litigation substantial sums could be recovered from some or all of the

defendants, that fact alone would not have made it the duty of the directors to authorize the commencement of an action. It would have made it their duty to weigh the advantages of a probable recovery against the cost in money, time and disruption of the business of the company which litigation would entail. It appears from the nature of the litigation, the variety and complexity of the issues, the period of time during which the asserted frauds allegedly were committed, the multitude of transaction between the two corporations, the many individuals involved, and the questions of accounting, that the directors were confronted with litigation of formidable proportions. Many directors, other than those named as defendants herein, were also accused in general terms of conspiracy and fraud. A mistake of judgment on the part of a board of directors does not justify taking the control of corporate affairs from the board of directors and placing it with the stockholders. The board of directors may make incorrect decisions, as well as correct ones, so long as it is faithful to the corporation and uses its best business judgment.",

and at pages 178-179 (Cal.) and 431 (Pac.)

"There was no manifest breach of duty in its decision not to commence an action." The board exercised its business judgment. Under such circumstances, a stockholder may not usurp the discretionary powers of the managers of the corporation by commencing a derivative action. If, under such circumstances, the court should entertain such an action it would be substituting its own busi-

ness judgment for that of the directors. The determination of the matter by the board of directors is a bar to the action herein."

The California court, in *Levinson v. Cosmosart Realty & Bldg. Corp.* (1929), 96 Cal. App. 549 at 557, 274 Pac. 597 at 600, says:

"In the absence of fraud, breach of trust or transactions which are *ultra vires*, the conduct of directors in the management of the affairs of a corporation is not subject to attack by minority stockholders in a suit at equity, where such acts are discretionary and are performed in good faith, reasonably believing them to be for the best interest of the corporation. (14 Cor. Jur. 927, sec. 1444; 6 Fletcher, *supra*, p. 6924, sec. 4065, p. 6707, sec. 3902, p. 6951, sec. 4086; *Rogers v. Nashville etc. Ry. Co.*, 91 Fed. 299.)".

and at page 558 (Cal.) and 600 (Pac.) quoting from a New York case says:

"To warrant interference by a court in favor of minority stockholders . . . a case must be made out which plainly shows that such action is so far opposed to the true interests of the corporation itself as to lead to the clear inference that no one thus acting could have been influenced by any honest desire to secure such interest, but that he must have acted with an intent to subserve some outside purpose, regardless of the consequences to the company."

In Delaware Cases.

With respect to Delaware, this rule is well stated in *Davis v. Louisville Gas & Electric Co.* (1928), 16 Del.

Ch. 157; 142 Atl. 654; where the court says (142 Atl. 654 at pages 659-660):

"We have then a conflict in view between the responsible managers of a corporation and an overwhelming majority of its stockholders on the one hand and a dissenting minority on the other—a conflict touching matters of business policy, such as has occasioned innumerable applications to courts to intervene and determine which of the two conflicting views should prevail. The response which courts make to such applications is that it is not their function to resolve for corporations questions of policy and business management. The directors are chosen to pass upon such questions and their judgment unless shown to be tainted with fraud is accepted as final. The judgment of the directors of corporations enjoys the benefit of a presumption that it was formed in good faith and was designed to promote the best interests of the corporation they serve.

In *Bodell v. General Gas & Electric Corp.*, 15 Del. Ch. 420, 140 Atl. 264, the Supreme Court of this state said:

'If in the particular case there is nothing to show that the directors did not exercise their discretion for what they believed to be the best interest of the corporation, certainly an honest mistake of business judgment should not be reviewable by the court.'

The same principle was recognized by Delaware in *Hilo Chemical & Dye Corp. v. Steel & Tube Co. of America*, 14 Del. Ch. 1; 120 A. 480; *Id.*, 14 Del. Ch. 64; 122 A. 142; and expressly

stated in *Robinson v. Pittsburgh Oil Refining Co.*, 14 Del. Ch. 193; 126 A. 46.)

Apparently in challenge to these authorities, the Petition repeatedly cites *Pepper v. Litton*, 308 U. S. 295, and *Rogers v. Hill*, 289 U. S. 582 (Pet. pp. 4, 12, 16, 18, etc.) and the related case of *Rogers v. Guaranty Trust Co.*, 288 U. S. 123. These cases are not directly relevant except as they may discuss general principles of equity. They are federal cases and unless they purported to apply the law of either California or Delaware, could not be even indirectly applicable, and they do not so purport to apply the law of either of such states. They differ radically from the present situation on their facts and issues. *Pepper v. Litton* involved the powers of a bankruptcy court charged with protecting the interest of creditors, in determining priority and validity of claims for royalties and other payments made by the dominant figure of a one-man corporation which was part of a clear, though complicated, scheme to defraud the creditors. *Rogers v. Hill* presented primarily the question as to the validity of a by-law of the American Tobacco Company authorizing payment of percentages of the net profits of the company to certain officers as bonus payments, and the reasonableness of the payments made under that by-law in view of changed conditions. This was a case in the first instance of corporate power to adopt such a by-law under the laws of the state of incorporation, and subsequently whether the huge resulting bonuses could have any reasonable relationship to the value of services. The case was remanded to determine the latter issue. The related case of *Rogers v. Guaranty Trust Co.*, 288 U. S. 123, was an attack by a stockholder to

determine the validity of an issue of shares of the corporation to selected employees under the laws of the state of incorporation, *i.e.*, a question of corporate power in which the action brought in New York had been dismissed without prejudice as a discretionary matter on the ground that an action in the state of incorporation would be a more convenient forum. This Court affirmed the dismissal without prejudice by the trial court.

Pepper v. Litton seems primarily cited by Petitioner by way of argument that once a plaintiff challenges a director in a derivative suit, then the burden of proving the good faith of the transaction and its inherent fairness is on the director. The matter of burden of proof in a diversity case has been held by this Court to be governed by state law. (*Guaranty Trust Co. v. York*, 326 U. S. 99 at 109, 65 S. Ct. 1464; *City Service Oil Co. v. Dunlap*, 308 U. S. 208, 60 S. Ct. 201.) In the case at bar, evidence was adduced over two lengthy trials which did prove the good faith, the inherent fairness and the reasonableness of the contracts involved. The rule as to burden of proof in both California and Delaware is shown by the cases already cited, and they would control if they actually differ from *Pepper v. Litton*, but since the evidence *was* presented and could only come from the defendants, there is no issue of burden of proof here involved.

Petitioner, again with reference to *Pepper v. Litton*, cites (Pet. p. 4, Footnote 1) *Kemerson v. Burbank Amusement Co.*, 120 Cal. App. 2d 157, 260 P. 2d 823, to show that *Pepper* actually represents the law of California. The *Kemerson* case was an action against a corporation on an employment contract in

which the primary question was whether it was *ultra vires* the corporation for a Board of Directors to delegate substantially all its powers to an employee by contract. These cases do discuss general equitable principles involving the fiduciary status of directors of a corporation, but Petitioner's attempt to rely thereon is in total disregard of the facts as reflected in the Findings, and disregards the fact that such Findings justify the judgment under the much more pointed and parallel state authorities already cited.

In the case of *Alexander v. Tennessee Valley Authority*, 297 U.S. 288, 56 S. Ct. 466, this Court had before it a derivative suit which, however, did not depend upon diversity, and held that one reason why the plaintiff therein had a right to proceed was (297 U.S. 318) because he was not merely challenging the right of the Board of Directors to exercise its business judgment. This indicates the general federal acceptance of the so-called Business Judgment Rule, an acceptance of which is further reflected in the former Opinion of the Court in the present case when it said that a trial on the merits may show a dispute lying in the penumbra of business judgment unaffected by fraud. Fraud as so used in such Opinion, obviously means the presence of an improper influence or an imposition of a will antagonistic to the interest of the corporation itself which would prevent the exercise of that business judgment from being true, fair and independent.

This case, therefore, presents an instance where after two lengthy trials a court has found all the necessary elements which enter into the acceptance by a court of the business judgment of the corporation itself. All of the elements that determine that the business judg-

ment used herein was actually independent and proper have been found, and those elements are the elements which the courts of Delaware, of California and of the United States accept as determinative. It is submitted, therefore, as previously indicated, that Petitioner now seeks only a redetermination of whether the evidence supports those detailed and complete Findings.

Conclusion.

It is submitted that Petitioner has shown no reason whatever for the issuance by this Court of a Writ of Certiorari. There is no federal or constitutional question involved. There is no new question of general importance or interest or any conflict of authority. This Court, upon its former consideration, indicated that the trial which was ordered might show a case lying within the scope of the Business Judgment Rule, and the Findings of the trial court show that such a situation does exist, which Findings have been twice reviewed by the Court of Appeals and found to have adequate support in the record.

Respectively submitted,

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FREEDMAN & FELIX,

H. R. KELLY,

Of Counsel.

XXV.

The Court finds with reference to each of said agreements described in paragraphs XXIII and XXIV hereof that the same was executed in the due course of the business of Warner Bros., was executed in each case on behalf of Warner Bros. by officers thereunto duly authorized; that said agreements, and each of them, were approved by the Board of Directors of Warner Bros., either at the time or by subsequent action; that the Board of Directors, which in each case approved each of such agreements, was free from control or domination by any of the individual defendants herein, or any alleged wrongdoer; that each of said agreements was duly considered in good faith by said Board of Directors and, in passing upon and approving or ratifying each of said agreements, the said Board of Directors and the members thereof, exercised its and their independent business judgment without fraud, coercion or domination.

That the contracts, amendments and agreements described in paragraphs XXIII and XXIV of these Findings, and each and all of them, were made and entered into in good faith and without fraud and were fair and reasonable; that said contracts, amendments and agreements, and each and all of them, were intended by the directors of Warner Bros. to be of financial benefit to said corporation and its stockholders; and said contracts, amendments and agreements, and each and all of them, were considered by the eleven members of the Board of Directors of Warner Bros. to be sound business arrangements for the best, present and

future interests of the Corporation that its approving and authorizing said contracts, amendments and agreements, and each and all of them, the officers and Board of Directors acted in good faith and exercised their independent business judgment. That neither the stockholders nor officers or directors of Warner Bros. were, at any time involved in this action, antagonistic to the interests of the Corporation.

XXVI.

The Court further finds that during the trial of this action the plaintiff has raised issues not presented by the pleadings having to do with matters of interpretation of the agreements herein involved and accounting practices with relation thereto which involve essentially the following matters:

(a) Claim that the method of the recoupment of the loss sustained by the parties hereto in connection with the picture "My Girl Friday" was erroneous and that the interpretation of the contract under which said recoupment was made was also erroneous;

(b) That by reason of delays in production of pictures the defendant Sperling received salary over a longer period of time than he should have and in consequence Warner Bros. was required to bear a larger amount of such salary than was contemplated by the parties;

(c) That the charging of the loss on the abandoned literary properties to overhead allocable to pictures produced was erroneous; and

(d) That miscellaneous items of United overhead consisting principally of sums paid as attorneys' fees

and to certain employees of United, were improperly allocated to overhead instead of to direct cost of pictures and that thereby Warner Bros. was deprived of payment of its overhead upon such items.

XXVII.

The Court finds that during the course of the trial, at the suggestion of the Court, the plaintiff elected to present and did present the claims asserted by the Complaint herein, and, in addition thereto, each of the matters referred to in the immediately preceding paragraph of these Findings, in writing, to the Board of Directors of Warner Bros. for its action with reference thereto; that said Board of Directors duly considered each of the claims asserted by the plaintiff herein, had an independent investigation made thereof, received a report of such investigation, duly considered and discussed each of such claims and said report and, thereafter, on motion duly made and seconded, said Board unanimously adopted the following resolution:

"Resolved: That due consideration having been given to the letter of October 10, 1958, referring to the lawsuit entitled Smith v. Sperling, et al., signed by counsel for the plaintiff, the letter of October 29, 1958, signed by counsel for Warner Bros. Pictures, Inc., Harry M. Warner and Jack L. Warner, defendants in the lawsuit, and the report of November 21, 1958, signed by Messrs. Donovan, Leisure, Newton & Irvine, counsel retained by the Board to investigate the law and facts and report with their recommendations

"It is the considered judgment of this Board, in view of all the circumstances, that

(1) it is not in the best interests of the Corporation to lend its sanction to proceedings in the pending

action entitled Smith vs. Sperling, et al., seeking cancellation of the agreement of September 28, 1945, with United States Pictures, Inc.; and

(2) it is not in the best interests of the Corporation to lend its sanction to any proceedings against the Estate of Harry M. Warner, Jack L. Warner, Milton Sperling or United States Pictures, Inc., in the pending action entitled Smith vs. Sperling, et al., either as included in the present complaint or in said complaint if amended to include any of the matters set forth in the letter of October 10, 1958; and

(3) it is not in the best interests of the Corporation to institute any legal proceedings against the Estate of Harry M. Warner, Jack L. Warner, Milton Sperling or United States Pictures, Inc., with respect to the matters set forth in the letter of October 10, 1958;

"Further Resolved: That the Secretary be instructed to reply to the letter of October 10, 1958, by sending to the writer a copy of that portion of the minutes of the meeting of October 24, 1958, and of this meeting, which relate to said letter, together with a copy of the report of November 21, 1958, of Messrs. Donovan, Leisure, Newton & Irvine."

The Court finds that at the time of the adoption of said resolution the Board of Directors of Warner Bros. consisted of nine members, of whom eight were present; that seven only, of said members considered the matters referred to by the plaintiff herein and the report of the Board's investigation thereon and voted thereon. That the members of said Board of Directors who voted were Charles Allen, J. L. Wobbill Catchings, Stanleigh P. Friedman, Benj. Kalmenson, W. J. Mur-

R. W. Perkins and Serge Semenenko. That the defendant, Jack L. Warner, a member of said Board, was not present at said meeting; that his brother Albert was present but did not participate in the discussion or vote with reference to such matters.

The Court finds that the said Board of Directors acted in good faith, without fraud, coercion or domination of any person or persons whatsoever; that in considering and passing upon said matters said Board and the members thereof intended to and did act in the interest of Warner Bros. and exercised its and their independent business judgment; and that its and their decision, as above set forth, was the exercise by it and them of such independent business judgment; that such matters were matters properly before said Board and properly the subject of the exercise by it of its said independent business judgment.

COPY

IN THE

Supreme Court of the United States

October Term, 1960

No. 245

CHARLES B. SMITH, as Special Administrator of the Estate of Edward S. Birn, Deceased,

Petitioner,

vs.

MILTON SPERLING, JACK L. WARNER, UNITED STATES PICTURES, INC., WARNER BROS. PICTURES, INC., and HERBERT FRESTON, MILTON SPERLING, REA E. WARNER and DORIS WARNER VIDOR AS EXECUTORS OF THE ESTATE OF HARRY M. WARNER, DECEASED,

Respondents.

PETITIONER'S REPLY.

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